
**TRANSFER
PRICING
DEFINED**

Transfer Pricing, within Pacific Bell, is the provisioning of non-tariffed goods and services and Intellectual Property/Proprietary Information (IP/PI) under written agreement between Pacific Bell and its affiliates.

A "*Transfer Price*" is a monetary value assigned to any goods, services and IP/PI exchanged between the individual business segments of a consolidated entity. Within a regulated environment, Transfer Pricing ensures an arm's length relationship between Pacific Bell, Pacific Telesis Group and Affiliates. Transfer Pricing prevents cross-subsidization between Pacific Bell and Pacific Telesis Group or Affiliates. It requires separate management accountability for revenues and expenses for each entity.

**AUDITS
AND
CONTROLS**

The process of billing for nontariffed goods and services and Intellectual Property/Proprietary Information, IP/PI, provided to Pacific Telesis Group and Affiliates is subject to audits by Pacific Bell internal auditors, the contracting companies (Affiliate) internal auditors, each company's external independent auditors, and the auditors of any of the regulatory bodies.

Internal and external auditors rely on our ability to produce documents that substantiate our compliance with Affiliate Transaction and Transfer Pricing Guidelines. Since audits take place months after activities have started, documentation of all services and transfer of IP/PI should provide sufficient detail to substantiate a transaction at a later date.

**INTERNAL
REVIEW**

An internal review of the controls that govern Transfer Pricing is conducted at least annually within Pacific Bell. This review is conducted as a part of the Pacific Bell Compliance Program. You may be requested to participate in the review. If you are requested to participate, it is your responsibility to provide any needed information. You will be notified of your involvement in the review.

**Transfer Pricing
Administration**

The Transfer Pricing Administration Network is composed of:

- Transfer Pricing Affiliates Group (TPAG)
- Regulatory
- Pacific Telesis Legal Group (PTLG)
- Business/Support Unit Single-Point-of-Contact (SPOCs)
- Business Controls Managers
- Internal Auditors
- External Auditors
- Pacific Bell Employee Body

This network is responsible for designing and implementing the methods and procedures required to ensure compliance with Affiliate Transactions and Transfer Pricing. The specific responsibilities of each group are listed below. In addition, some basic responsibilities of all Pacific Bell employees are provided.

**Transfer Pricing
Affiliates Group
(TPAG)**

The Transfer Pricing Affiliates Group (TPAG) is the organization responsible for the administration of Transfer Pricing within Pacific Bell. Within this group there are Transfer Pricing Administrators (TPA), Methods and Practices (M&P) managers, and Billing Associates.

Responsibilities

The ongoing responsibilities of TPAG are:

- Oversee Transfer Pricing within Pacific Bell
- Develop Methods and Procedures for Transfer Pricing within Pacific Bell
- Implement Transfer Pricing between Pacific Bell and any affiliate company.
- Identify the organizations involved in providing services to the affiliate company
- Inform each organization involved in Transfer Pricing of the need to establish a single-point-of-contact for Transfer Pricing
- Coordinate and monitor the identification of services to be transfer priced
- Coordinate the execution and signing of the General Administrative Services Agreement (GASA), the Master Intellectual Property and Licensing Agreement, and the Schedules (service agreements or contracts)

Responsibilities
(Con't)

- Provide a central point of contact for Transfer Pricing within Pacific Bell
- Provide the expertise for identifying and costing service components
- Maintain the Transfer Pricing System (TPS)
- Monitor existing contracts, and coordinate renegotiations, renewals and terminations (cancellation)
- Interface with the affiliate, Regulatory, Legal, Pacific Telesis Group Affiliate Transaction Governance, and Auditors on all Transfer Pricing related issues
- Provide for dispute resolution where the dispute impacts all or most affiliate companies
- Handle non-billing related issues raised by the Pacific Telesis Group companies receiving services
- Prepare Transfer Pricing Bills. Monitor billing to ensure that monthly services are billed each month. Ensure all bills received by Pacific Bell affiliates and subsidiaries are covered by contract. Ensure all bills received by Pacific Bell Affiliates and subsidiaries are processed through the system within two billing cycles
- Oversee new affiliate formation activities and ensure compliance with rules and regulations
- Prepare reports for Regulatory to submit to the FCC and the CPUC
- Prepare section 5 of the Cost Allocation Manual (CAM)

Transfer Pricing Administrator (TPA) The TPA represents Pacific Bell's interest on all matters relating to an organization's contracted services. There are TPAs assigned to every organization within Pacific Bell. (See Appendix D)

The TPA's responsibilities are:

- Prepare Schedule(s) and Manual(s) for services
- Coordinate the implementation of cost collection procedures used for reporting billed expenses Coordinate additions, changes and renewals
- Provide for dispute resolution of items relating to Schedules and billing
- Provide for record retention
- Perform costing

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TPAs (Con't)

- Oversee billing
- Determine the most accurate procedure to bill the administrative costs of performing the Transfer Pricing function

Methods &
Procedures
(M&P) Managers

The M&P managers are responsible for designing and implementing the methods and procedures associated with all aspects of Affiliate Transactions and Transfer pricing.

The M&P responsibilities are:

- Develop the Methods and Procedures for implementing the Pacific Telesis Group "Affiliate Transactions Policies, Guidelines and Reporting Requirements" within Pacific Bell
- Develop Methods and Procedures for Intellectual Property and Proprietary Information
- Develop Methods and Procedures for costing of services
- Develop Methods and Procedures for billing
- Maintain the Transfer Pricing System
- Monitor Schedules and Manuals
- Coordinate Business Control Reviews
- Handle requests for information from various regulatory agencies
- Support testimony and audits
- Coordinate Market Price studies as required
- Manage new affiliate formation activities

Billing Associates

The Billing Associates execute the billing of all Transfer Pricing transactions on a monthly basis.

The Billing Associate's responsibilities are:

- Gather data for billing reported expenses
 - Process bills
 - Ensure billing is timely and accurate
 - Ensure proper billing backup is available
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Regulatory

The Regulatory Group is responsible for providing oversight, advice and counsel for the management of Affiliate Transactions and Transfer Pricing. It is their responsibility to ensure that all related activities comply with regulatory requirements and that all affiliate transactions obtain CPUC approval when required. (e.g. sale of Pacific Bell assets, leasing of Pacific Bell space, etc.)

**Pacific Telesis
Legal Group**

The Pacific Telesis Legal Group (PTLG) is contracted by Pacific Bell to be responsible for providing advice and counsel as well as to interpret laws which might impact Affiliate Transactions and Transfer Pricing. PTLG support may also be necessary whenever transactions between affiliates require special terms and conditions.

**Business/Support
Unit Single-Point
of-Contact**

Each Business or Support Unit within Pacific Bell should have a single-point-of-contact. The role of this individual is to assist in ensuring compliance with the rules and regulations governing Transfer Pricing. This person serves as the subject matter expert for Transfer Pricing within his/her organization. He/She assist the Transfer Pricing Administrators in identifying appropriate contacts for any services the department might be providing. (See Appendix C)

**Business Controls
Managers**

The Business Controls Managers reside in every Business/Support Unit within Pacific Bell. One of the roles of the Business Control Manager is to ensure that their organization is in compliance with the rules and regulations governing Transfer Pricing and IP/PI exchanges with affiliates. They assist in the review process and incorporate their results into the quarterly compliance review process that is a part of the Pacific Bell Compliance Program.

Internal Auditors

Internal Auditing perform audits of Affiliate Transactions and Transfer Pricing as a part of their Annual Audit Plan.

External Auditors The external auditors perform an annual audit which provides an opinion as to whether the methodology in place at Pacific Bell for Affiliate Transactions and Transfer Pricing are in conformance with the FCC approved Cost Allocation Manual and whether the reported results are an accurate application of those methodologies.

All Employees

All employees within Pacific Bell are responsible for:

- Knowing when they are dealing with an affiliate employee
- Knowing that they cannot provide goods and/or services and IP/PI to that affiliate without a Transfer Pricing Agreement (Schedule/Service Contract) in place
- Knowing there are some affiliates that have more stringent requirements for receiving services including regulatory approval.
- Reporting their time and expenses accurately when providing goods and/or services to an affiliate
- Being aware that there are added costs associated with Transfer Pricing
- Understanding the importance of serving the affiliate in a timely and quality manner
- Participating in review/audit process when asked to do so

In general, employees should be aware of:

- Our success and ability to change regulation is contingent upon our ability to comply with the rules and regulations governing Affiliate Transactions and Transfer Pricing
- The task of providing affiliate service includes ensuring that our affiliates (except Nevada Bell and Pacific Bell Directory) are charged the higher of Fully Distributed Costs plus 10% (surcharge mandated by the CPUC) or Market Rate
- Every employee is directly accountable for the continued health of the company, not just by doing their work well, but by accounting for it correctly

TRANSFER PRICING

WHEN DO YOU DO IT? HOW DO YOU DO IT?

PURPOSE

The purpose of this section is to outline the responsibilities of each "service provider" within Pacific Bell. It is important for you to be familiar with these rules and make sure to follow them for any affiliate transaction in which you participate.

BACKGROUND

Each organization within Pacific Bell has the potential to provide goods/services and Intellectual Property/Proprietary Information (IP/PI) to its affiliates. There are certain requirements that must be followed in order to ensure that Pacific Bell is in compliance with state and federal laws, as well as regulatory policies governing transfer pricing. It is important to understand the Company's commitment to manage affiliate transactions properly, following both the letter and spirit of the rules. These rules include the following:

- Reporting time properly
 - Recording and tracking any shared Proprietary Information (see Section 4 for more information)
 - Receiving proper authorization prior to transferring assets to an affiliate (see Section 3 for more information).
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TRANSFER PRICING AND YOU

Transfer Pricing guidelines apply to all employees of Pacific Bell, salaried and non salaried. As an employee of Pacific Bell, you are responsible for ensuring that we comply with the requirements of transfer pricing. This includes:

- Knowing when you are talking to an employee of an affiliate company (To get the most current list of affiliates call 1(800)337-9200)
- Ensuring that a Transfer Pricing Agreement (Schedule/Service Contract) is in place (signed by both Pacific Bell and the client) before you provide any goods or services to the client

TRANSFER PRICING AND YOU CAN'T

- Accurately reporting the time you spend providing a service to an affiliate within the Pacific Telesis Group so that the affiliate can be billed correctly
 - Notifying your Transfer Pricing Administrator (TPA) (See Appendix D) when changes occur which impact the integrity of the Service Agreement (Contract) and the billing of the service. (See section 2, page 6.)
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What To Do When An Affiliate Requests Services

When you receive a call requesting goods or services, the first thing to do is to establish whether the caller works for Pacific Bell or an affiliate. Remember, never take for granted that he/she are an employee of Pacific Bell.

Find out what goods or services the client is interested in receiving. Indicate that you will have to investigate to ensure that you can do business with the prospective client and that you will get back to him/her as soon as possible.

Prior to providing the service, Pacific Bell must decide if it is in the best interest of the Company to do so. (See Section 2, Page 8.) If it is, then a Transfer Pricing Agreement (Schedule/Service Contract) must be put in place with the affiliate before providing any goods or services.

NOTE: Each affiliate company must have its own agreement in order to obtain goods and services from Pacific Bell.

Can I Provide Goods and Services to Any Affiliate Within the Pacific Telesis Group?

Generally, all affiliates within the Pacific Telesis Group can receive goods and services from Pacific Bell. However, there are some restrictions for certain affiliates. Decision 92-07-072 states that services provided to Pacific Bell Information Services (PBIS) are limited to those that are defined as "*critical or essential*". In addition the 1996 Telecomm Act sets forth guidelines pertaining to the provisioning of services to required affiliates, e.g. the long distance company, Pacific Bell Communications, as well as Pacific Bell Interactive Media. Before providing services to any affiliate, you must check with the Transfer Pricing Administrator (TPA) (See Appendix D) to determine if the affiliate is limited by "*critical or essential*" or the Telecomm Act. In some cases regulatory approval may be required before the service is offered, or you may be precluded from providing the service altogether.

**Putting A Schedule
/Service Contract
In Place**

Non-tariffed goods and services may be provided by Pacific Bell to most affiliates but only under written agreement. Within Pacific Bell, this written agreement or service contract is called the Schedule. To get a Schedule in place, call your Transfer Pricing Administrator (TPA). (See Appendix D - List of TPAs) Let the TPA know that your organization is interested in doing business with an affiliate. Using section 1, page 7, as a reference, provide the TPA with all of the information required for putting a Schedule in place.

The TPA will work with you and the affiliate to ensure that an agreement is put in place in a timely manner. If the service is complex, or if the affiliate has specific requirements, you may be requested by the client to provide an attachment to the schedule that outlines the Performance Criteria for both the providing and receiving parties. Section 1, Appendix A addresses the Performance Criteria attachment to the Schedule.

Once the Schedule is written and signed by both parties, you may begin providing goods and services.

Under no circumstances should you begin providing goods and/or services without a signed agreement.

NOTE: Identical services may be provided to a number of different affiliates. However, each affiliate must have its own signed Schedule in place before Pacific Bell may begin providing service.

**What Price Do I
Quote If An
Affiliate Asks
For the Cost of
The Service**

Pacific Bell must be compensated for providing services to its affiliates. The costing methodology employed, has generally been derived from Accounting Letters A-6 and A-15, the Comptrollers Letters M237 and M328, and the Pacific Telesis Group "Affiliate Transactions Policies, Guidelines and Reporting Requirements" (Appendix A).

**What Price Do I
Quote If An
Affiliate Asks
For the Cost of
The Services
Con't**

For the purposes of Affiliate Transactions and Transfer Pricing, "telco" refers to Pacific Bell, Pacific Bell Directory and Nevada Bell and "non-telco" refers to all other Pacific Telesis Group affiliates, including the Pacific Telesis Group and Pacific Bell Category III Below-the-Line affiliates.

NOTE: A Pacific Bell Category III Below-the-Line affiliate is a company which is subject to California Public Utilities Commission (CPUC) categorization rules, which provide competitive services, has maximum product pricing flexibility and whose earnings are not included in the determination of sharing under California's incentive regulation process.

For the purpose of pricing, it is important to understand that affiliates fall into two categories "telco" and "non-telco". Costing guidelines for these two entities are somewhat different.

**Using the
Correct Costing
Methodology**

Sales from Pacific Bell to a **telco** affiliate: For **telco**, the Fully Distributed Cost Method, excluding a 10% CPUC surcharge, will be used to price goods and services

Sales from Pacific Bell to a **non-telco** affiliate: For **non-telco**, price will be computed using the Fully Distributed Cost Method plus a 10% CPUC surcharge or Market Price whichever is **higher** (when market price is determinable at a reasonable cost).

**Fully Distributed
Cost Method**

All costs associated with providing the service are incorporated under this method. These costs include:

- Primary Expenses
- Direct Expenses (e.g., out-of-pocket)
- Overhead Costs
- Expense-related loadings
- Investment-related loadings
- Transfer Pricing overhead rate (TPOR)
- Float
- CPUC 10% Surcharge

NOTE: There is a ten percent (10%) surcharge that has been imposed on Transfer Pricing by the California Public Utilities Commission, Decision No. 86-01-026. This surcharge applies to all non-telco affiliates when billing is based on the Fully Distributed Cost Method.

Market Price

Pacific Bell is required to determine market price for each specific service it provides to non-telco affiliates when there is an annual aggregate billing, for those particular services, to all affiliates in excess of \$100,000 (excluding billings to Pacific Bell Directory and Nevada Bell). The studies are to be completed no more than 180 days after Pacific Bell determines, or should have determined, the \$100K threshold has been met. Non-telco affiliates shall continue to be charged FDC plus 10% during the study period.

If the results of the study are that market price is higher than FDC plus 10%, Pacific Bell is required to bill retroactively the non-telco affiliate (retroactive to the beginning of the year in which the \$100K threshold was reached). The amount billed is the difference between FDC plus 10% and market price, plus applicable interest (using the average 90 day commercial paper interest rate). If FDC is higher, Pacific Bell continues to bill the affiliate at the FDC +10% rate. (See Section 5)

NOTE: The affiliate company will be required to absorb the cost of any Market Price Studies which must be performed.

Get Your Transfer Pricing Administrator Involved

To ensure that the correct cost is quoted to an affiliate, it is highly imperative that you involve your Transfer Pricing Administrator when an affiliate requests a service from you.

Ongoing Responsibilities Once the Schedule Is Signed

Your responsibilities do not stop once the Schedule is signed and you begin providing services. As the service provider, you have an ongoing responsibility to your client to ensure that it is receiving the service it requested in a quality, as well as timely manner. It is your responsibility to understand the billing components of the service and to notify both the TPA (See Appendix D) and the client when those components change. Changes in billing components may impact the amount we charge the client and therefore must be monitored constantly. This is to ensure that the client has the opportunity to review the impact of the billing changes and to cancel the service if desired.

In addition, if Performance Criteria have been agreed to, these too must be monitored to ensure that all changes are communicated to the client.

**How Do I Impact
Billing of An
Affiliate?**

Pacific Bell's ability to correctly capture the costs of each service provided to an affiliate is imperative to doing business. Inaccurate costing of a service can put Pacific Bell at risk of noncompliance, as well as result in backbilling to the client. Reconstructing billing information is time consuming and costly to Pacific Bell and can result in unbudgeted costs for the affiliate, including interest charges.

It is the responsibility of the service provider to ensure that all costs are correctly identified when a service is initiated. This includes identifying all of the billing components and how each of those components will be priced or expensed.

During the life of the service, it is the responsibility of the service provider to ensure that any changes in components or methods of capturing costs are communicated to the Transfer Pricing Administrator (See Appendix D). This includes but is not limited to:

- Changes in the description of service, including additional or fewer service components.
- Changes in billing components, especially if each component uses a different billing methodology
- Changes in codes used to capture costs, e.g., Function Codes, ARCs, Tracking Codes, etc.

IDENTIFYING THE SERVICE

Description of Service(s)

Describe in detail the service that will be provided to the affiliate.

Personnel to Perform the Service(s)

Identify all personnel that will be involved in providing the service, e.g., two engineers, one staff associate, etc. List the associated ARC's and Job Function Codes (JFCs).

Location of Service(s)

Identify the location(s) where the service will be provided. (e.g., leasing of space would require the street addresses and possibly room numbers, floors and/or cubicle numbers of employees leasing space.)

NOTE: Approval must be obtained from the affiliate transactions oversight committee (ATOC) (See section 3, page 2). An 851 filing must be completed prior to putting a service contract in place.

Deliverables and Associated Materials to be Provided

Describe the expected deliverables and any associated materials that need to be provided to perform the service(s). If the service is very complex, you may be required to complete the Performance Criteria for attachment to the Schedule.

Schedule of Services

Describe how often this service will be provided (e.g., on a monthly basis, as requested by the client, etc.)

Compensation/Rates and Charges

Briefly describe how Pacific Bell will be compensated for the service(s) (How will you capture the costs for each component of the service, e.g., hours the service is performed for client, number of position I.D.'s for CDC, square footage of floor space, etc.?). Will there be a requirement for additional tracking mechanisms, (e.g., Interdepartmental Tracking Code, Job Function Code, Report Code, Project Time Accounting (PTA) Code, etc.)? Is the service considered investment intensive i.e., utilizes more than \$100K of investment in total (not just the affiliates portion of the service) e.g., systems used for billing of Pacific Bell equipment.

If the affiliate requests a quote for goods and/or services, make sure your Transfer Pricing Administrator has reviewed the costing methodology, loadings, and 10% CPUC surcharge before communicating the quote.

Invoices/Billing Information

This will typically be the responsibility of your Transfer Pricing Administrator. Note the name, telephone number and affiliate name of the employee(s) requesting service.

Service Manager/Point of Contact:

Who is responsible for the employees providing this service? Who can speak to the day-to-day operational matters? Who will be responsible for providing the Transfer Pricing Administrator with any changes that impact the service (e.g., changes in service description, number of employees performing the service, ARCs and other billing information, etc.)? Who will monitor the service? Who will answer questions related to tracking the costs of the service? Who will sign the Schedule/Service Contract? List names and telephone numbers here.

Status Reports/Progress Meetings

If required, who will manage the Performance Criteria and ensure that progress meetings are scheduled with the client if needed and/or as Performance Criteria changes? List names and telephone numbers here.

Reimbursable Expenses

What other reimbursable expenses might this service incur, (e.g., travel expenses, lodging, meals, consultant expenses, third party contractors, etc.)?

Other

List any other pertinent information.

IDENTIFYING THE SERVICE

Description of Service(s)

Personnel to Perform the Service(s)

Location(s) of Service(s)

Deliverables and Associated Materials to be Provided

Schedule of Services

Compensation/Rates and Charges

Invoices/Billing Information

Service Manager/Point of Contact:

Status Reports/Progress Meetings

Reimbursable Expenses

Other

PERFORMANCE CRITERIA
TO BE ISSUED

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AFFILIATE/SUBSIDIARY FORMATION ACTIVITIES

(pre-formation and post formation)

Purpose

The purpose of this section is to outline the responsibilities involved in affiliate/subsidiary formation, as well as activities that might result after separation.

General

Creating a new affiliate/subsidiary involves many considerations. Some are straight forward while others pose their own set of problems when associated with a separation from Pacific Bell. These considerations include:

- Tracking of Affiliate/Subsidiary Formation Activities
- Co-Location
- Sale of assets
- Leasing of assets
- Force Group Transfers

To ensure proper compliance with legal and regulatory requirements time and planning are required before forming an affiliate/subsidiary. It is extremely important that the expertise of the Transfer Pricing Affiliate Group (TPAG) be sought as early as possible in the formation process. This ensures that your efforts relative to formation proceed smoothly and that you are able to accomplish the formation on the date of your choice. Failure to include TPAG in the initial planning stage can jeopardize their ability to accommodate your requirements for separation.

Tracking for Affiliate Formation

Any time an activity occurs that could ultimately result in affiliate formation, an Interdepartmental Tracking Code must be established to capture the costs of that activity. All affiliate formation activities must be tracked and billed to the affiliate no later than the second billing cycle after separation occurs.

**Co-Location
Of An Affiliate/
Subsidiary On
Pacific Bell
Property**

The co-location of personnel from regulated and non-regulated Companies requires particular care. Such situations must be reviewed for appropriate controls before they are undertaken. This includes co-locations that may occur because of new affiliate formations as well as those which might occur after separation to meet the ongoing needs of the business.

To that end, no co-location of regulated and non-regulated forces is permitted without explicit approval from the Affiliate Transactions Oversight Committee (ATOC).

NOTE: If a force group transfers to a new organization (e.g., Pacific Bell to an affiliate) but remains in a Pacific Bell location, it is considered a co-location and must be approved under this policy.

To obtain authorization for co-location, you must submit a written proposal to: Pacific Telesis Regulatory Affairs, 130 Kearny St., Room 3008, San Francisco, California, 94108. The proposal should include:

- A description of the force groups involved; number of employees
- Address and owner of the space to be co-located
- Anticipated duration of co-location
- Rationale for co-location versus separate quarters
- Anticipated interaction between regulated and non-regulated force groups, including any proprietary information to be shared
- Description of any assets to be leased, e.g., computers, furniture, etc.
- Description of any assets to be shared, e.g., copiers, facsimiles, etc.
- Specific controls you will implement to ensure Affiliate Transactions rules will be adhered to by the groups involved

**Sale of Assets
(Equipment, Real
Property)**

Special rules apply to the sale of assets. If the asset is no longer needed by Pacific Bell to perform the day-to-day operations of the business, CPUC permission is not required. However, if the asset is still needed or useful to the operation of Pacific Bell, CPUC permission (under California PU Code Section 851) is required and a request (filing) must be submitted.

Pacific Bell must notify the CPUC 30 days in advance of the sale of any asset sale with a fair market value of \$100,000 or greater to an affiliate (Decision 87-12-067).

SALE OF EQUIPMENT

Equipment includes physical assets (other than real property) bought for use in the business. Equipment includes, but is not limited to, furniture, terminal equipment, personal computers and central office equipment.

**Sales From Telco
Affiliate to a
Non-Telco Affiliate**

Sales from a telco affiliate to a non-telco affiliate shall be priced at the higher of net book value plus the seller's incremental transaction cost or fair market value.

**Sales Between Telco
Affiliates**

Sales between telco affiliates shall be priced at net book value plus the seller's incremental transaction cost.

**Sales From Non-
Telco Affiliate
to a Telco Affiliate**

Sales from non-telco affiliates to telco affiliates shall be priced at the lower of net book value or fair market value.

SALE OF REAL PROPERTY

Real Property includes land and any improvements thereon, such as buildings (including capital improvements to the buildings).

**Sales From Telco
Affiliate to a
Non-Telco Affiliate**

Sales from a telco affiliate to a non-telco affiliate shall be priced at either net book value plus seller's incremental transaction cost or fair market value, whichever is higher. For sales from Pacific Bell, fair market value shall be established by competitive bid. The use of competitive bid is required by the CPUC (Decision 86-01-026, Ordering Paragraph 8).

**Real Property
Rights**

A real property right is the right offered by one affiliate to another to purchase real property (e.g., an option).

TRANSFER OF REAL PROPERTY RIGHTS

Transfer of real property rights from telco affiliates to non-telco affiliates shall be at market price. For transfers from Pacific Bell, market price shall be established using an independent appraisal. The use of an independent appraisal is required by the CPUC (Decision 87-12-067, Ordering Paragraph 34c).

The independent appraisal shall consider the following:

- The relationship of the party exercising the option to Pacific Bell or Pacific Bell Directory.
- The Selling price of the property if Pacific Bell or Pacific Bell Directory vacated the property.
- The Lease rate of the property if Pacific Bell or Pacific Bell Directory vacated the property.

**Transfer of Real
Property From
Non-Telco
Affiliates to Telco
Affiliates**

The transfer of real property from non-telco affiliates to telco affiliates shall be at market price.

**Transfer of
Property
Between Telco
Affiliates**

Shall be within the constraints of legal and regulatory requirements and shall incorporate those terms and conditions agreed upon by the negotiating Telco affiliates, provided such terms are not less than the seller's incremental cost of the transaction.

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Leases	Leases are agreements that convey the right to use tangible or intangible assets, normally property, plant or equipment, usually for a specified period of time, and establish the terms and conditions of such conveyance.
Leases <u>From</u> Telco Affiliates <u>To</u> Non-Telco	Shall be priced at either FDC plus 10% or market price, whichever is higher.
Force Group Transfers	The permanent movement of work group(s) from Pacific Bell to a non-regulated affiliate requires affiliate transactions, transfer pricing contracts, and Memos of Understanding (MOU) prior to the move.
Employee Transfers <u>From</u> Pacific Bell <u>To</u> Non-Telco	Employee transfers require a 25% fee based on the transferred employee's starting annual salary at the new company.

NOTE: Transfers from non-telco to telco affiliates, and transfers between telco affiliates do not require the 25% fee.

For more detailed information see Pacific Telesis "Affiliate Transactions Policies, Guidelines and Reporting Requirements" (Appendix A).

**INTELLECTUAL PROPERTY
(Including
PROPRIETARY INFORMATION)**

**PROCESSING
REQUESTS (con't)**

- Provide the appropriate Non-Disclosure agreement for the recipient's signature before the IP/PI is released and send copies of signed non-disclosure agreements to Pacific Bell Regulatory as required.
- Post all transactions on department IP/PI logs in accordance with regulatory requirements.
- If needed, follow-up with the TPAG to confirm that the information released has been billed to the affiliate

**EXCEPTIONS TO THE
RULE**

Currently, PBIS may only receive "critical or essential" information from Pacific Bell. **This rule may also apply to affiliates formed in the future.** Therefore, the department IP/PI SPOC must check with the Transfer Pricing Affiliates Group (TPAG) and/or Pacific Bell Regulatory before releasing IP or PI to PBIS (and possibly other affiliates formed after the date this instruction is published).

Additionally, all requests for IP and PI for **Pacific Bell Communications (PBC)** must be cleared through Pacific Bell Regulatory and the Pacific Telesis Legal Group (PTLG) before sharing can occur. And, due to legal constraints, Pacific Bell **cannot share any information with Pacific Bell Interactive Media (PBIM).**

**DETERMINING THE
VALUE OF IP/PI
SHARED WITH:**

**NON-TELCO
AFFILIATES**

The CPUC has mandated that Pacific Bell be reimbursed the higher of either fully distributed cost (FDC/fully loaded cost) plus a 10% surcharge or the market price. Because of the uniqueness of our business, often there is no practical way to determine a market price for IP/PI. You will need the assistance of your department's IP/PI SPOC and the Transfer Pricing Affiliates Group staff to determine: 1) if there is a market price for the information and, 2) the fully distributed cost which is a combination of the base cost to produce the information plus overhead loadings plus a 10% surcharge, and 3) the portion of the cost to be allocated to the affiliate. (e.g., if one affiliate wants the information, it would be charged 50% of the cost, if two affiliates want it, they would be charged 33% each.)

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**INTELLECTUAL PROPERTY
(Including
PROPRIETARY INFORMATION)**

TELCO AFFILIATES

Telco affiliates do not have to pay the 10% surcharge, but still must reimburse Pacific Bell for not less than the incremental cost of the information. Telcos are usually charged a portion of the FDC allocated based on relevant criteria such as head count or number of access lines. Logging is not required for exchanges with Telco affiliates but a Non-disclosure Agreement is required when PI is exchanged.

**IF AN INTER-DEPART-
MENTAL TRACKING
CODE WAS USED
DURING INFO
DEVELOPMENT**

If the information requested was developed by employees who report their time to an Inter-Departmental Tracking Code, special handling is required for billing. Please notify your SPOC and TPAG. Special handling of these requests will insure that the rate base for tariffed services is properly stated. Failure to notify the TPAG about the use of an Inter-Departmental Tracking Code could result in revenue and expense reporting mistakes.

HOW IS IP/PI BILLED?

Bills are rendered by the CWO unit based on billing information input to the Transfer Pricing System. For exchanges of Intellectual Property (IP) or Proprietary Information (PI) not integral to providing contracted services, Non-Telco affiliates are billed on the basis of FDC plus a 10% surcharge or market price, which ever is higher. Telco affiliates pay the FDC (excluding the 10% surcharge).

The IP/PI Logs, as discussed below, will be used as a basis for billing Non-Telco affiliates in the Transfer Pricing System.

**WHO PROCESSES THE
BILLING?**

IP and PI are billed as Affiliate Transactions. That means that the Transfer Pricing Affiliates Group (TPAG) processes the billing for these transactions. Below are the steps involved in billing for IP or PI:

1. The TPAG staff will verify if the request is associated with an existing service contract between Pacific Bell and the requesting affiliate and, if so, determine if the request is integral to the service description in the contract. If not, the Master Intellectual Property Agreement with that affiliate will

**INTELLECTUAL PROPERTY
(Including
PROPRIETARY INFORMATION)**

**WHO PROCESSES THE
BILLING? (con't)**

be checked to determine if the request falls into a preapproved category for sharing. If information is not covered under the pre-approved categories of sharing, a new Sharing Agreement will be prepared and routed for signature;

2. The TPAG staff will assist the departmental IP/PI SPOC in assigning a monetary value to the information. The pricing depends on whether the affiliate is a Telco or Non-Telco affiliate. See above "HOW IP/PI IS BILLED" for the differences in valuing.
3. Billing information is input to the Transfer Pricing System and processed through CWO billing. A paper bill is produced by the CWO unit and forwarded to Corporate Accounting Operations where it is mailed to the affiliate. TPAG provides billing detail to affiliates upon request.

JOB AIDS:

See Appendix D of this instruction for the following job aids:

**IP/PI SHARING
CHECKLIST**

For your convenience, there is a IP/PI Sharing Checklist in Appendix D, **EXHIBIT 1**. The purpose of the checklist is to provide a "to-do" list for handling requests for IP/PI.

**DOCUMENTING IP/PI
EXCHANGES**

EXHIBIT 2 - Proprietary Information/Intellectual Property Log Field Instructions - this exhibit provides the IP/PI SPOC with detailed instructions for logging, examples and a blank log form.

EXHIBIT 3 - IP/PI Sharing Agreement Worksheet - this form is used by the department IP/PI SPOC to identify the categories of IP/PI that the department is willing to share with affiliates. The form is forwarded to the TPAG for use in updating the Master Intellectual Property License Agreement Pacific Bell with pre-approved categories for sharing with each affiliate. After the License Agreement is updated, it will be routed to VP level for signature. The department form should be reviewed annually and updated if necessary. A sample IP/PI Sharing Agreement Worksheet is provided in Exhibit 3A.